

BEFORE THE DEPARTMENT OF ADMINISTRATION
OF THE STATE OF MONTANA

In the matter of the adoption of New)	NOTICE OF PUBLIC HEARING ON
Rules I through IV pertaining to financial)	PROPOSED ADOPTION
responsibility of mortgage loan)	
originators and control persons and)	
ultimate equity owners of mortgage)	
entities)	

TO: All Concerned Persons

1. On November 3, 2011, at 10:00 a.m., a public hearing will be held in Room 342 of the Park Avenue Building, 301 S. Park, Helena, Montana, to consider the proposed adoption of the above-stated rules.

2. The Department of Administration will make reasonable accommodations for persons with disabilities who wish to participate in this public hearing or need an alternative accessible format of this notice. If you require an accommodation, contact the Department of Administration no later than 5:00 p.m. on October 26, 2011, to advise us of the nature of the accommodation that you need. Please contact Wayne Johnston, Division of Banking and Financial Institutions, P.O. Box 200546, Helena, Montana 59620-0546; telephone (406) 841-2918; TDD (406) 444-1421; facsimile (406) 841-2930; or e-mail to banking@mt.gov.

3. GENERAL STATEMENT OF REASONABLE NECESSITY: Section 32-9-120(1)(c), MCA, requires the department to deny a license application if an applicant for a mortgage loan originator license has not demonstrated financial responsibility, character, and general fitness to command the confidence of the community and warrant a determination that the mortgage broker, mortgage lender, or mortgage loan originator will operate honestly, fairly, and efficiently within the purposes of the Montana Mortgage Act (Act). The control persons and ultimate equity owners of entities are held to the same standard pursuant to 32-9-113, MCA.

On August 29, 2011, the U.S. Department of Housing and Urban Development (HUD) adopted final rules to implement the Secure and Fair Enforcement for Mortgage Licensing Act of 2008, 12 USC 5101, et seq. (SAFE Act). Those proposed rules provide, in relevant part:

§ 3400.105 Minimum loan originator license requirements. For an individual to be eligible for a loan originator license required under § 3400.103(a) and (d), a State must require and find, at a minimum, that an individual:

(2)(c) Has demonstrated financial responsibility, character, and general fitness, such as to command the confidence of the community and to warrant a determination that the loan originator will operate

honestly, fairly, and efficiently, under reasonable standards established by the individual State.

HUD has required that the state develop reasonable standards to determine whether an applicant has demonstrated financial responsibility and will operate honestly, fairly, and efficiently. The state must develop those standards and enforce them in order to comply with the SAFE Act.

The department initially proposed a rule to implement 32-9-120(1)(c) and 32-9-127, MCA, on August 13, 2009, in MAR Notice 2-59-414 published in 2009 Montana Administrative Register, Issue Number 15 at page 1292. In response to the comments received in that rulemaking, the department is proposing a new rule.

The comments received in response to the new rule proposed in MAR Notice 2-59-414 were largely that the mortgage industry, like the country as a whole, has fallen on hard times. The commenters were concerned that the state of the economy could prevent a mortgage loan originator from becoming licensed. Several people commented that business is way down, and the people who are still in the mortgage broker or lender industry are having economic difficulties. They commented that a person who lost a home due to being unable to afford the payments should not be prevented from being a mortgage loan originator.

Some people commented that the department should not adopt a rule implementing 32-9-120(1)(c) and 32-9-127, MCA. The department does not have that option. The SAFE Act and the Act mandate the department to determine whether an applicant has demonstrated financial responsibility and will operate honestly, fairly, and efficiently within the purposes of the law.

In order to license individuals as mortgage loan originators and control persons or ultimate equity owners of entities, the department must comply with 32-9-120(1)(c), MCA. In fairness to applicants who may have unpaid tax liens or other government liens, foreclosures, or unpaid debts, the department must define the standard and give guidance to applicants as to how that standard will be applied and what the effect of financial issues will be on licensure.

In drafting this rule, the department reviewed the financial responsibility rules of several other states and ultimately decided to pattern its financial responsibility after the Idaho policy because it seems closest in line with the attitudes and influences in Montana. It is a reasonable policy that allows the individual to explain the adverse information on a credit report and rehabilitate the individual by entering into repayment agreements and faithfully paying toward debts owed.

The department will review the credit history of an applicant and, based on the totality of the credit history and the surrounding circumstances, including the explanation of the individual, if any, make the required determination as to whether the individual has demonstrated financial responsibility and will operate honestly, fairly, and efficiently within the purposes of the SAFE Act.

The history of and the reason(s) for unpaid debts are critical to this analysis, as well as what the individual is doing to satisfy the debt. For instance, if an individual has unpaid tax liens but that person has entered into a repayment agreement with the government, and has faithfully performed the obligations that have become due under the repayment agreement to date, that fact alone would not justify denial of a license.

In exercising its discretion under 32-9-120(1)(c), MCA, the department will consider the totality of the credit history, as well as any explanation or supporting documentation that the applicant submits to the department.

4. The new rules proposed to be adopted provide as follows:

NEW RULE I APPLICATION OF FINANCIAL STANDARDS (1) Section 32-9-120(1)(c) and 32-9-113, MCA, require mortgage loan originators, as well as ultimate equity owners and control persons of entities, to meet financial responsibility standards. These persons are referenced in [NEW RULES I through IV] as "individuals."

(2) Financial responsibility, character, and general fitness are continuing requirements for individuals and must be met at all times including upon initial licensure and renewal.

AUTH: 32-9-130, MCA

IMP: 32-9-113, 32-9-117, 32-9-120, 32-9-166, MCA

STATEMENT OF REASONABLE NECESSITY: The Act makes the standards of financial responsibility, character, and general fitness a requirement for licensure and for renewal of licenses. 32-9-120, MCA. In addition, the Act requires the control persons and ultimate equity owners of entities to meet the same standards in order for the entity to become licensed. 32-9-113, MCA. The purpose of (1) is to define "individuals" as used in the remainder of these rules.

Section (2) provides that the financial standards, character, and general fitness standards are continuing standards the applicant must meet at the time of the application, at the time of renewal, and at all times in between. See 32-9-113, 32-9-117, and 32-9-120, MCA. The standards are the subject of several disclosure questions that applicants must answer on the Nationwide Mortgage Licensing System (NMLS). The NMLS requires applicants and licensees to update their responses to disclosure questions and keep them current, accurate, and complete under penalty of perjury and unsworn falsification to authorities. In addition, 32-9-166, MCA, provides that a licensee shall file a written report with the department within 30 business days of any material change to the information provided in a licensee's application. Therefore, the financial, character, and general fitness standards are continuing ones.

NEW RULE II STANDARDS FOR DETERMINING FINANCIAL RESPONSIBILITY (1) The department shall find an individual lacks the required financial responsibility if a pattern of disregard is shown regarding the management of the individual's personal financial affairs.

(2) In determining whether an individual has shown a pattern of disregard regarding their own personal financial affairs, the department shall consider the following factors:

- (a) the existence of outstanding judgment(s), excluding judgments resulting solely from medical expenses;
- (b) the existence of outstanding tax liens or other government liens or filings;

- (c) a pattern of delinquency in child support or student loan payments;
 - (d) the existence of outstanding collection actions against the individual unless solely as a result of medical expenses;
 - (e) the existence of outstanding charged-off accounts with a remaining past due balance owed unless solely as a result of medical expenses;
 - (f) the existence of three or more accounts currently 90 days or more past due; and
 - (g) a foreclosure within the past three years.
- (3) The department may not consider a bankruptcy as the sole basis for a finding that an individual lacks the required financial responsibility; however, the department may consider the factors that lead to the bankruptcy.

AUTH: 32-9-130, MCA

IMP: 32-9-113, 32-9-117, 32-9-120, MCA

STATEMENT OF REASONABLE NECESSITY: The general standard, a pattern of disregard for the management of personal financial affairs, comes from the model law developed by the Conference of State Bank Supervisors and the American Association of Residential Mortgage Regulators to implement the SAFE Act. The SAFE Act requires that a credit report be obtained from a consumer reporting agency for each applicant for a license as a mortgage loan originator. When the model act was developed, the drafters agreed that the purpose of requiring a credit report from applicants was to determine financial responsibility. Since this standard is the model law adopted by 44 states, the department feels it is appropriate to base its rules on the same standard. In addition, another goal of the SAFE Act was to promote uniformity, which is also furthered by this rule.

The model law is as follows:

CHARACTER AND FITNESS—The applicant has demonstrated financial responsibility, character, and general fitness such as to command the confidence of the community and to warrant a determination that the mortgage loan originator will operate honestly, fairly, and efficiently within the purposes of this Act.

(a) For purposes of this subsection a person has shown that he or she is not financially responsible when he or she has shown a disregard in the management of his or her own financial condition. A determination that an individual has not shown financial responsibility may include, but not be limited to:

- (i) Current outstanding judgments, except judgments solely as a result of medical expenses;
- (ii) Current outstanding tax liens or other government liens and filings;
- (iii) Foreclosures within the past three years;
- (iv) A pattern of seriously delinquent accounts within the past three years.

NEW RULE II(2)(a), (b), and (g) incorporate into factors (i), (ii), and (iii) listed in the model law. The appearance on credit reports of the factors in (2)(c), (d), (e), and (f) would cause the department concern regarding an individual's financial responsibility. The department views these matters as serious enough to warrant an inquiry of the individual as to what happened and why these debts have not been paid.

Federal law prohibits a bankruptcy from being the sole basis of a denial of licensure. 11 USC 525. However, the licensing entity may take into consideration the behavior underlying a bankruptcy in determining an applicant's past and future financial responsibility.

Since an individual has no control over medical issues that can result in overwhelming medical bills, any and all debt related to medical expenses is excluded from a financial responsibility analysis.

NEW RULE III PROCEDURES FOR DETERMINING FINANCIAL RESPONSIBILITY (1) If an individual's credit report or response to any application disclosure question contains adverse information, the department shall:

(a) notify the individual in writing of the specific items that must be addressed; and

(b) specify the documentation that must be provided for the department's consideration and review.

(2) Examples of the type of documentation that the department may request include, but are not limited to, the following:

(a) a written explanation of the circumstances surrounding the adverse information reported; and

(b) documents that the department finds necessary for its review of the adverse information including, but not limited to, copies of:

(i) satisfactions of judgment;

(ii) bankruptcy discharge orders, schedules, or dismissal documents;

(iii) satisfactions of outstanding tax liens or other governmental liens;

(iv) court documents showing the factual basis underlying the adverse information being reviewed by the department and how the matter was resolved or adjudicated; and

(v) account statements or letters from the individual's creditors, or lien or judgment holders, explaining and verifying the current status of any past due accounts, including documentation of any repayment plans and agreements, as well as any temporary or permanent modifications to such accounts.

(3) Any document provided must be legible and complete. Incomplete documents may not be accepted.

(4) If the individual is unable to obtain the documents the department requests, the individual shall support that fact with documentation from the source of the unavailable documents consisting of a written statement from the agency or creditor who holds or held the records. The statement must be:

(a) written on the agency's or creditor's letterhead indicating that:

(i) the agency or creditor does not have any record of the matter;

(ii) the record was lost, damaged, or destroyed, or cannot otherwise be produced; and

- (iii) the reason why the information is not available;
- (b) signed by the agency's or creditor's records custodian; and
- (c) include contact information such as phone number, mailing address, or e-mail address.

(4) Applications must be deemed withdrawn or abandoned if the applicant fails to provide the information requested by the department within 60 days of notification to the applicant by the department of deficiencies in the application or December 31, whichever comes first.

AUTH: 32-9-130, MCA

IMP: 32-9-113, 32-9-117, 32-9-120, MCA

STATEMENT OF REASONABLE NECESSITY: If the department finds one or more matters on a credit report or a disclosure question that raises concerns regarding financial responsibility, the department will notify the individual as to which matters are cause for regulatory concern and request that the individual explain what happened and why the debts are unpaid or provide evidence that the debts have been paid or that the individual has entered into a repayment agreement with the creditor and is making a good faith effort to meet the terms of the repayment agreement. The reason for this is that the individual must be given notice of the matters that raise concerns for the department and be given the chance to explain those matters. Credit reports can be wrong, or simply outdated, and the applicant must be given the opportunity to provide to the department any additional information the applicant would like to provide relevant to the matters of concern.

If the debt has been paid or discharged, the department requires documentary evidence of that. The rule lists the type of documentary evidence which will be required. The department requires actual documentary evidence, not simply a statement from the individual that the debt has been paid, in order to assure that the debtor and creditor agree on the current status of the debt.

If the individual cannot produce the records requested by the department, (4) sets forth the types of documents which must be produced to evidence that fact. A letter from an applicant saying that the creditor cannot locate the debt is not sufficient; the letter must come from the creditor and have sufficient evidence of reliability to be acceptable. The department requires documentation from the creditor, not the applicant, in order to ensure accurate and correct information.

Sometimes, after the department requests additional information, the individual does not respond or provide additional information. Then the department has to make repeated efforts to contact the individual in an effort to determine what the person intends to do. In an effort to avoid this situation, the department is proposing to deem an application withdrawn or abandoned for failure to provide the requested information to the department within 60 days of the request or December 31, whichever comes first. December 31 is the date that all licenses expire. Applications are rarely submitted from November 1 to December 31 because that is the dedicated period of license renewal. Any applicant that submits an initial application for licensure during the renewal period must also renew the license by December 31, provided that the license is issued by that date. This does not penalize the applicant for failing to respond; the applicant is free to reapply at any

time in the future with no negative consequence from the withdrawn application. It will allow the applicant to work to improve their financial responsibility without a negative sanction attaching to their license.

The other option for the department would be to deny the license because the factors required to issue a license under 32-9-120, MCA, cannot be found in the application provided by the individual. This is an unnecessarily harsh result for an applicant who filed an application and failed to complete it. A denial of a license would have to be reported on all subsequent applications and explained. This result should be reserved for more egregious conduct than failing to complete an application.

NEW RULE IV REVIEWING ADVERSE CREDIT HISTORY AND OTHER INFORMATION (1) In making a determination whether an applicant has demonstrated financial responsibility, character, and general fitness, the department shall consider the following:

- (a) the individual's credit history reflected in a credit report;
- (b) supplemental information and documentation requested from and provided by the individual as determined necessary by the department;
- (c) responses and information contained in the individual's application filings;
- (d) previous and current license history with the department, to include any regulatory actions that have occurred;
- (e) other information that reflects upon the financial responsibility, character, and general fitness, whether favorably or adversely;
- (f) the timing and context of the information reviewed;
- (g) patterns of conduct; and
- (h) factors indicating that financially adverse information may be the result of the involuntary loss of job or income, divorce, or health issues. Under such circumstances, the individual shall provide documents showing attempted workout arrangements with creditors or other factors indicating the individual has made an attempt to correct his or her financial difficulties.

(2) The department may not base a license application denial solely on a license applicant's credit score.

(3) In determining financial responsibility, the department shall consider the totality of the applicant's credit history, and surrounding circumstances, in exercising its discretion under 32-9-120(1)(c), MCA.

(4) Although the following is not an exclusive list, the department may consider the following factors, or a combination thereof, in determining whether to deny, condition, suspend, or revoke a license. The individual:

- (a) has failed to fully provide any documentation required by the department;
- (b) has made a false attestation associated with a filing related to an application for a license or a license renewal;
- (c) has failed to pay in full any past due account, lien, judgment, or charged-off balance either as of the date of the issuance of a credit report to the department, or at time of initial licensure, designation as a control person or ultimate equity owner, or at renewal of any license. In reviewing this factor, the department shall make an exception for any account, lien, judgment, or charged-off balance that is solely due to medical expenses;

(d) is in arrears or has failed to comply with the terms of a repayment plan or agreement entered into with a creditor;

(e) has failed to make timely payments under a plan or agreement with any state or federal tax or other regulatory agency; and

(f) has any of the factors listed in [NEW RULE II(2)].

AUTH: 32-9-130, MCA

IMP: 32-9-113, 32-9-117, 32-9-120, MCA

STATEMENT OF REASONABLE NECESSITY: The decision whether to issue, deny, condition, suspend, or revoke a license based on financial responsibility is grounded on the totality of the circumstances. It is not susceptible to a bright line test; however, the factors that will and will not be considered are listed. As a matter of fairness, the department must consider all the factors before it in making a licensing decision, including aggravating and mitigating factors for the behavior in question. Each case must be decided on its own merits within the framework established by statutes and rules. In so doing, the department has determined that the factors listed in NEW RULE IV(1) are indicative of the factors which, if they exist, may be relevant to the licensing decision. The factors will not be viewed in isolation but will be viewed as a whole.

Credit scores alone are not a factor in the decision; however, the behavior that led to a particular credit score can be a factor in determining financial responsibility. Many loan originators believe that the department bases licensing decisions on credit scores. This is not so. The credit score is simply a number and cannot be used to determine whether the individual in question has demonstrated financial responsibility. The crux of the matter is an analysis of what is going on in the individual's life that may provide extenuating circumstances for a pattern of unpaid debts or not, as the case may be. That requires the department to define the factors that will be considered, or not considered, in making a licensing determination.

The factors listed in this new rule are designed to give the applicant notice of the types of factors that will be considered by regulators in assessing financial responsibility. The department will review the individual's credit history as revealed in the credit report since that is required by the SAFE Act. In addition, the department will consider the additional information and documentation received from the individual in response to an inquiry from the department. Obviously, the individual's explanation will be very important in determining extenuating factors or aggravating factors in any credit issues. The department will review all other answers and information provided by the individual in the application for licensure. Specifically the department will look at financial disclosure questions included within the application for licensure. Any affirmative responses provided by the applicants on the financial disclosure questions require the applicants to provide additional documentation. Any false or misleading responses or failure to disclose information in response to financial disclosure questions will be viewed negatively.

In addition, the department will consider the individual's prior and current regulatory history with the department as a factor in the licensing decision. For instance, an individual who has a history of noncompliance with the Act will be dealt

with more harshly than someone who has no prior regulatory history. In fairness, the department will consider any other information it has that reflects either positively or negatively on the individual's financial responsibility, character, and general fitness. The department will take into account the age and repetitive nature of any conduct at issue. A remote unpaid debt does not raise the same regulatory concern as a new unpaid debt. A single unpaid debt generally, although not always, is not of the same degree of regulatory concern as a pattern of unpaid debts. However, a large unpaid debt may rise to a significant level of regulatory concern.

If an individual provides a reasonable explanation for how the financial difficulties occurred, such as job loss, divorce, or health issues, the department will then look for a repayment agreement and evidence that it is being met in determining whether the individual is making a good faith effort to pay the debts despite difficult financial conditions. The department realizes that things happen in an individual's life that can lead to financial difficulties. The intent of this rule is not to penalize an individual because something unfortunate has happened. The intent of the rule is to distinguish between someone who falls on hard times but still makes an effort to pay their debts, who should be licensed, and someone who has a willful pattern of nonpayments of debts, who should not.

As noted, the department will not base its decision to deny a license solely on a credit score. A credit score is an arbitrary number assigned by a credit rating agency. It is not helpful to the regulatory analysis of financial responsibility which requires an analysis of the reasons for an individual's financial condition, and bona fide attempts to meet financial responsibilities in spite of hardships, or conversely, a willful pattern of unpaid debts. Every licensing decision is fundamentally a discretionary decision based on the totality of the circumstances that each separate application presents.

In determining whether to deny, condition, suspend, or revoke a license, the department will take into account all the factors present in the particular license application including any failure to fully provide any documentation required by the department or false attestation associated with a filing related to an application for a license or a license renewal. The department will view these two factors extremely negatively. In fact, the financial responsibility issue becomes secondary to character and fitness when an applicant makes a false attestation or fails to fully provide documents to the department.

The department will also consider whether the individual has failed to pay in full any past due account, lien, judgment, or charged-off balance either as of the date of the issuance of a credit report to the department, or at time of initial licensure, designation as a control person or ultimate equity owner, or at renewal of any license. The failure to pay a legitimate debt will be viewed negatively. In reviewing this factor, the department will make an exception for any account, lien, judgment, or charged-off balance that is solely due to medical expenses. The language regarding medical expenses is from the model law. The rationale is that an individual is able to control their spending but medical expenses cannot be controlled by an individual. The department agrees with this rationale.

The department will view negatively any individual who is in arrears or has failed to comply with the terms of a repayment plan or agreement entered into with a creditor or has failed to make timely payments under a plan or agreement with any

state or federal tax or other regulatory agency, unless a reasonable explanation is given for such failure. The department believes that these failures show a lack of financial responsibility, thus justifying the negative viewpoint.

In addition, the department will consider the factors set forth in NEW RULE II(2) for the same reasons as are listed in the statement of reasonable necessity under NEW RULE II.

5. Concerned persons may present their data, views, or arguments, either orally or in writing, at the hearing. Written data, views, or arguments may also be submitted to Kelly O'Sullivan, Legal Counsel, Division of Banking and Financial Institutions, P.O. Box 200546, Helena, Montana 59620-0546; faxed to the office at (406) 841-2930; or e-mailed to banking@mt.gov. The data, views, or arguments must be received no later than 5:00 p.m., November 14, 2011.

6. Kelly O'Sullivan, Legal Counsel, Division of Banking and Financial Institutions, has been designated to preside over and conduct the hearing.

7. An electronic copy of this Proposal Notice is available through the department's web site at <http://doa.mt.gov/administrativerules.mcp>. The department strives to make the electronic copy of the notice conform to the official version of the notice, as printed in the Montana Administrative Register, but advises all concerned persons that if a discrepancy exists between the official printed text of the notice and the electronic version of the notice, only the official printed text will be considered. In addition, although the department works to keep its web site accessible at all times, concerned persons should be aware that the web site may be unavailable during some periods, due to system maintenance or technical problems.

8. The Division of Banking and Financial Institutions maintains a list of interested persons who wish to receive notices of rulemaking actions proposed by this division. Persons who wish to have their name added to the mailing list shall make a written request which includes the name, mailing address, and e-mail address of the person to receive notices and specifies that the person wishes to receive notices regarding division rulemaking actions. Notices will be sent by e-mail unless a mailing preference is noted in the request. Such written requests may be mailed or delivered to Wayne Johnston, Division of Banking and Financial Institutions, 301 S. Park, Ste. 316, P.O. Box 200546, Helena, Montana 59620-0546; faxed to the office at (406) 841-2930; e-mailed to banking@mt.gov, or may be made by completing a request form at any rules hearing held by the department.

9. The bill sponsor contact requirements of 2-4-302, MCA, do not apply.

By: /s/ Janet R. Kelly
Janet R. Kelly, Director
Department of Administration

By: /s/ Michael P. Manion
Michael P. Manion, Rule Reviewer
Department of Administration

Certified to the Secretary of State October 3, 2011.